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**THE EFFECTS OF CREDIT CARD TOWARDS CUSTOMER SPENDING**

**BEHAVIOR**

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## DECLARATION

“I declare that this thesis is my own work except the citation and excerpts of each of which I have mentioned in the references.”

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## DEDICATION

The Final Year Project is dedicated to my parents for their loves, endless support, encouragement and prayers.

## ACKNOWLEDGEMENT

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## ABSTRACT

In Malaysia the credit card lending is keep increasing from time to time until now majority of professional, government servant and private servant are the credit card holder. One of the important contributions to this trend is that Malaysian consumers have displayed a positive move towards credit card facility. They are able to make loans for themselves. They also can obtain funds easily via credit card than personal loans with many documents procedures being relaxed

Compulsive purchasing without any control and tranquil source of obtaining credit has directed to various hostile concerns such as infatuation to unnecessary shopping and thus over leveraged debt. (BNM Report, 2010). According to a study, many Malaysian consumers have shown such a change in behavioral pattern. Since, credit card encourages the independent and reliable usage of credit to the cardholders to meet their future consumption in advance, this sight has also gives increase to debt default to indiscipline users. Hence, Debt alone could be seen to lettering off capital and trigger the excessive default rates which finally will results into the stability of an economy and invulnerability of the financial system. (Zafar U et al, 2010).

With this in attention, it is the purpose of this study to offer empirical results that could assist financial institution decision makers and regulators in firming up their capabilities for supervision of credit card management. This study aim to investigate the factors influence people to use credit card and to identify the effect of credit card towards customer spending behavior.

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## **CHAPTER 1**

### **INTRODUCTION**

#### **1.0 Introduction**

The controversial issues as been addressed by many experts not only in terms of the numbers of credit card flooding the nation's economy, but the payment default which endangered the economy and the amount of transactions that end up with the numbers of credit card fraud has been recorded should be seriously focused. However the progresses and exchanging habits in purchasing activities significantly contributed to the diffusion of credit card as becoming more relevant and important in continuing the purchasing activities.

This chapter evaluated about the background of the study and also discussed about the research question and research objective for this study. In this chapter the scope limitation in this study is explained. Besides that, the important of this research also emphasized in this chapter.

#### **1.1 Background of the Study**

The credit card exists since early 1950s and today it is widely used around the world especially in urbanized countries as payment system in order to transfer funds. It has been become a normal for everyone to purchase an item without the need for carrying large sum of paper money. Payment for goods and service through internet using credit cards has also gained recognition worldwide. So, the usage of credit cards has eliminated the need for carrying cash for purpose to purchase an item.

In Malaysia the credit card holders is keep increasing from time to time until now majority of professional, government servant and private servant are the credit card holder. One of the significant contributions to this trend is that Malaysian consumers have showed a positive move towards credit card facility. They are able to make loans for themselves. They also can obtain funds easily via credit card than personal loans with many documents procedures being relaxed.

Propagation of Islamic Credit Card has increased the last two decades, which is different from the conventional Credit card which operates on charges interest and loan basis. Islamic Credit Card is fully accommodating with Shari'ah principles but it is still provides the same reimbursements as conventional Credit. Nowadays, Islamic credit card has become attractive to both Muslims and nonMuslims. The Islamic credit card adds value attracts customers, both Muslims and nonMuslims due to its valuable services and features to the customers because of the application, concept, and low cost compared to conventional one.

Credit cards have several positive effects on customer spending behavior gaining for them many benefits and advantages. For instance, credit card can help the holders to keep track of their expenses, save their receipts and check them against their monthly statement. The secure device of credit card payment has gained trust and popularity worldwide. On the other hand, even though it has become a normal practice to own credit cards for variety of reasons, their effects are still uncertain both in developed and developing countries. These cards also have several negative effects such as for example overspending, fraud, default, and lack of awareness.

Among the newly developed nations, most of the credit cardholders are urban occupants, working as professionals and have a higher level of education. The explosion of credit cardholders has taken an insensitive spending by customers with numerous impacts. Perhaps, one of the major culprits for the ongoing financial crises is the wide-ranging grant of credit to the people. It was reported that next financial crises could be caused only because of the compulsive buying nature of credit card.

The early signal of the impact is excessive buying behavior which forces to purchase out of their common needs. Obsessive purchasing without any control and

relaxed source of obtaining credit has directed to various aggressive concerns such as infatuation to excessive shopping and thus over leveraged debt. Many Malaysian consumers have shown such a change in behavioral pattern according to a study. Since, credit card encourages the self-determining and reliable usage of credit to the card holders to meet their future consumption in advance, this sight has also gives rise to debt default to indiscipline users.

Hence, Debt alone could be seen to lettering off capital and trigger the excessive default rates which finally will results into the constancy of an economy and imperviousness of the financial system. One of the important strides in this regards is that Malaysian consumers has displayed a positive move towards the credit card facility. It is mainly because they able to grant loans for themselves. Meaning, they can obtain funds as easily than personal loans via credit card with many documents procedures being relaxed.

The card holders also have the option to decide whether to revolve on credit cards, how much to revolve within the assigned credit limits, and when to pay off their debts at their own ease. Due to the uncommitted and non-secured features of credit cards, credit card debt holders are more likely to default on credit card debt than other secured debts, such as car loans, installment loans, and home loans. In other words, since no warranty can be repossessed by the card issuers, barely any retrieval can be made from credit card debts once file bankruptcy or households default. Therefore, banks trade-off this risk by charging a service fees and high interest rate on credit card debt, making it more expensive for the customers to carry unsecured debt than secured debt. Due to heavy credit card spending and failing to settle their loans early on in their working lives, many employees have been declared bankrupt.

Amazingly, there have been very few efforts to measure the connection between levels of customers spending and credit card usage, perhaps because the endogeneity problem is so difficult to solve. Although prior cross-sectional research has found that consumers generally tend to spend more with credit cards than with cash, there are many reasons why this might be the case, including that people tend to pay for larger purchases with credit cards and for smaller purchases with cash or credit card users are different from users of cash.

Income and occupation are generally accepted as one of the most popular indicator that clarified and significantly correlates with the usage of credit card. But family income and education may be primary determinants of credit card usage. Better educated families and higher income were more possible to use credit cards than lower income families. In fact, the factor in defining of how much the purchasing power of consumers will be spent on goods or services was determined by incomes. This is because of high income consumers might have more favorable attitudes towards credit use because they have more capability to pay off their debts than low income consumers and they are also less likely to be credit inhibited.

One significant line of inquiry has focused not on whether credit cards promote spending, but on whether consumers under calculate their own credit card use and/or the level of credit card debt they will accumulate. A few studies have examined the customers' attitude towards their spending behavior when using credit cards. Most of these studies have focused on the customers' behavior of conventional credit card holders. Their focus has not taken into thought the acceptance and common usage of Islamic credit card by the public as additional to the conventional credit card, given the wide acceptance of Islamic banking practice in Malaysia. It would be interesting to see the style of behavior among the users of Islamic credit cards. It is expected that these users will be highly disciplined since Islamic banking products are based on ethical values.

## **1.2 Problem Statement**

With the significant growth of Debit cards used as an easy paying instrument, the protected mechanism of credit card payment has gain momentum, trust and popularity worldwide. Even though, it has become a normal practice to own credit cards for the variety of reasons and are increasing progressively, its impacts are still doubtful both in developed and developing countries.

The explosion of credit cardholders has taken an insensitive spending by customers with numerous impacts. Perhaps, one of the major culprits for the ongoing financial crises is the extensive grant of credit to the people. It was reported that the obsessive buying nature of credit card will caused the next financial.

(Business Week, 2011) The early signal of the impact is extreme buying behavior which compels to purchase out of their common needs. Obsessive purchasing without any control and tranquil source of obtaining credit has lead to various hostile concerns such as infatuation to excessive shopping and thus over leveraged debt. (BNM Report, 2010). According to a study, many Malaysian consumers have shown such a change in behavioral pattern. Since, credit card encourages the independent and consistent usage of credit to the cardholders to meet their future consumption in advance, this sight has also gives growth to debt default to indiscipline users. Hence, Debt alone could be seen to writing off capital and trigger the excessive default rates which finally will results into the stability of an economy and invulnerability of the financial system. (Zafar U et al, 2010). One of the substantial strides in this regards is that Malaysian consumers has showed a positive move towards the credit card facility. It is mainly because they able to grant loans for themselves. Meaning, they can obtain funds as easily than personal loans via credit card with many documents procedures being relaxed. As a result, credit cards issued till February 2012 rose to 10.1 million (BNM Report, 2010).

Importantly, the credit card holder is growing at a composite annual growth rate (CAGR) of 50.4% per annum in the past 7 years since 2005 in Malaysia which is the major concern of controlling authorities to lower down the debt ratio. In the year 2009, it was reported to have 11.41% of the total consumer credit which accounts for 1.35% of the total loans outstanding. Out of total 1.35%, nearly 6.43% of the amount outstanding has been written off as non-performing loans. Again in the next year, the amount of credit card debt showed increase reporting RM24.8 billion. (Bank Negara Malaysia, 2010) A shocking trend of credit card holders finally going through the bankruptcy stage was also stated. (Bank Negara Malaysia, 2011)

A minority of studies have observed the consumer spending behavior and attitude using credit card. Most of the studies studied the consumer behavior of conventional credit card holders. Due to the wider acceptance of Islamic banking practice in the Malaysian region, the Islamic credit card is promoted and become commonly used by the public as an alternative for conventional credit card. This study seeks to investigate whether the obsessive purchasing trend or excessive buying behavior via credit has also penetrating into the Islamic credit card holder

and if its confirmatory, then what extend they tend to depart with the conventional credit card holders (Zafar U et al, 2010).

Since finding the basic reasons of a problem delivers a good prospect of solving the problem and make further policy recommendation. In the wake of this discussion, this study would seek to investigate the credit card spending behavior of two categories of banking, conventional and Islamic. With this in attention, it is the purpose of this study to offer empirical results that could assist financial institution decision makers and regulators in firming up their competences for supervision of credit card management.

### **1.3 Research Question**

Research question was designed based on the research problem. In this research, the researcher have been stated in research problem where the obsessive purchasing without any control has directed to various hostile concerns such as infatuation to excessive shopping and thus over leveraged debt.

The concerns have been described in problem statement where to investigate whether the excessive buying behavior or compulsive purchasing trend via credit has also penetrating into the Islamic credit card holder and if its affirmative, then what extend they tend to deviate with the conventional credit card holders. Thus, this study would seek to investigate the credit card spending behavior of two categories of banking, conventional and Islamic.

Research Question:

- 1) What are the factors that influence people to use credit card?
- 2) What are the effects of credit card on customer spending behavior?

## **1.4 Research Objectives**

The research objective was designed based on the research topic and research problems. Research objective playing an important role in the research to make sure the research is always on the track. In this research,

### **Objectives of the Study**

- 1) This study aims to investigate the factors that influence people to use credit card.
- 2) To identify the effects of credit card towards customer spending behavior.

## **1.5 Scope and Limitation**

The research is about the effect of credit cards toward customers' spending behavior. The main purpose of this research is to identify the factors influence people to use credit card and understand the attitude of Malaysian credit card holders toward spending and settlement behavior.

The focus group in this research is among a population in Melaka, Selangor and Kuala Lumpur representing people age 19 years old and above. Those who have career were represented as the respondents because they meet the required criteria, using credit cards either conventional or Islamic. This research purposely chosen Melaka, Selangor and Kuala Lumpur because the researcher believes the most of credit card holders living in this area represent the high-income group. The researcher conducts survey by distributing questionnaires to the number of respondents.

As for the limitation for the research, the time and cost are the limitation endured by researcher. Besides that, given that this research is quantitative, there is a need to embark on in-depth study (qualitative) to understand the effect of credit cards on customers' spending behavior in much better way.



## **1.6 Importance of study**

The findings are expected to be significant to financial institutions catering the service of credit cards, as they pave a reference to senior management to have a considerate level of knowledge about the credit cardholders in Malaysia and thus can be reasoned to make policy recommendation as to the spending behavior of both conventional and Islamic credit holder. This study should be considered the first of its kind to be conducted in the banking sectors which offer the factors that influence people to use credit card and the effects of credit card towards customers spending behavior in Malaysia.

Thus, the area of such comparison would propagate concern not only to Policy makers such like regulators, but also to various stake holders like shareholders, Bank managers, existing literature and Muslim Ummah in general. The shariah compliance aspect is relevant or not relevant to both type of consumers can be assessed where by the shariah scholar could draw shariah compliance consciousness among them. It is of prime interest to the regulators as well as to quantify the quantitative and qualitative aspects of credit card spending behavior to gauge the future financial obligation of the public.

## **CHAPTER 2**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

A literature review is a body of text that aims to review the critical points of current knowledge on a particular topic. Literature review are secondary sources, and as such do not report any new or original experimental work. Literature search was to perform studies, implementation, factor and analyzing the research of student acceptance toward paperless classroom to enhance green education in university in Melaka. This section also will review the suitable tool and method used in the research. This chapter will explain all the terminology used and certain of importance definition.

#### **2.2 The Background of Study**

##### **2.2.1 Customer Spending**

###### **2.2.1.1 Behavior**

According to Merriam-Webster, behavior defines as the way a person or animal acts or behaves. Behavior also refers to the response and reaction of an individual, group, or species to its environment.

### **2.2.1.2 Human Behavior**

According to psychology glossary, “human behavior refers to the full range of physical and emotional behaviors that human involve in biologically, socially, intellectually and influenced by culture, attitude, emotions, values, ethics, authority, rapport, persuasion, pressure and genetic”. In another side, from the Theory of Reasoned Action (TRA), an individual behavior is determined by individual intention to perform the behavior, and this intention is influenced by the individual’s attitude.

In addition, based on Business Dictionary, human behavior define as the capacity of mental, physical, emotional, and social activities experienced during the five stages of a human being life including prenatal, infancy, childhood adolescence, and adulthood.

### **2.2.1.3 The concept of Spending**

Customer spending is one of the elements of behavioral change. Behavioral change defines as any conversion of modification of human behavior. It involves how customers react with the environment changes. Spending has been conceptualized as an outcome variable in a psychological process that customers go through in making decision about the technology and environment changes (Andrew D. & Michael G.M., 1996).

In this research, the researchers want to study are the factors influence people to use credit card and the customers spending behavior when using credit card as payment mechanism. The researchers have to understand the dynamic of human decision in the concept of spending or shopping using different payment mechanism which is credit cards. It is required customers to spend or shopping their goods or any products using credit cards instead of using cash money. It is something that customer’s willingness to use credit cards as payment mechanism when spending their goods or service. In order to identify the effect of credit cards on customers spending behavior, the researchers must identify and understand the advantage and disadvantage of credit cards to know the factor of different customers

spending behavior. Researchers also need to identify both of Islamic credit cards and conventional credit cards and the benefit to the customers.

From these, as theory and related to customer spending behavior is emerged, the researchers use PESTLE analysis to study the factors influence people to use credit card and the effect of credit cards toward customers spending behavior. It helps researchers to understand customers spending behavior include attitude and intention paradigm to predict the customers' preferences towards credit cards.

### **2.2.2 Facts about Credit Cards**

Based on the previous article, The Bank Negara Malaysia defined credit card as a card issued by a financial company giving the holder an option to borrow funds, usually at point of sale. Credit cards charge interest and are mainly used for short-term financing. Interest usually begins one month after a purchase is made and using limits are pre-set according to the individual's credit rating. For many reasons, credit cards were preferred by many people to make the purchases in their daily life. Hence, credit cards issuers, especially banks, have entered into aggressive competition in the credit card market that is rapidly growing. Having a credit card can be a brilliant convenience. In this day and age, it's hard to imagine living without one. But without self-discipline, a credit card can actually cause more harm than good. We've all heard stories about people paining up enormous amount of credit card debt and struggling to get out of it.

Back to the history, credit cards were first issued at the beginning of the 20th century, by hotels in the United States. By 1914, the credit cards trends also influence the departmental stores and gas station that make them also distributing credit cards. The third party cards which act as entertainment and travel cards appeared in the 1950's and eventually the bankcard appeared. In the 1960's, Bank America Card distributed the first bankcard or now known as Visa card. Master Charge systems and Visa in the United States had established themselves as the bank's credit card industry in order to avoid the competition during that time (Garcia, 1980).

Credit card, which was also known as plastic money, their usage has gone up intensely around the globe since they have been announced. In the early of twentieth century, credit cards were first distributed in the USA. Since then, they have become very common in many countries in the world that the credit cards are the major system for exchange of transactions or payments that stimulates household and personal spending (Watkins, 2000).

In Malaysia, credit cards were first announced in the mid-1970s in Malaysia (Loke, 2007). At the early stage, credit cards were not distributed to everyone and it was only issued to those professionals and successful businesspersons by card distributing companies. There were approximately 20,000 cards were distributed by the end of 1970s. During that time, holding a credit card was considered a symbol of prestige as only the wealthy people have the chances to own the credit card.

Basically, credit cards in Malaysia can be separated into three categories. Each type of cards having their own purposes and offer to different users, they are classic card, gold card, and the platinum card. People that have consistent income or low credit ratings will use the Classic card. Meanwhile, Gold card are offer to people with good income level or strong credit ratings and the gold card also provide a wide range of reward programs. Lastly, only the wealthy people or by special invitation only can own the platinum card. It comes with convenience services and having some high-class offers with airlines, premiere hotels and restaurants.

Credit card can be said as the most common financial transaction intermediaries around the world, and this same goes to Malaysia too. This statement can be showed by volume of credit card transaction and value of credit card transactions in Malaysia keep increasing from year 2005 till year 2017. In my research, my focus is study about the credit card usage among Malaysians. Nowadays, it is a common phenomenon that everyone bring a credit card with them wherever they go, but, the problems is, most of the credit cards user did not know how to use the credit cards wisely. Hence, there been lots of issue with the credit cards users that dealing with the debt problems or if more serious they will face the bankruptcy at the end.

But with more than 200 different types of credit cards presented by banks in Malaysia, it is no wonder Malaysians are confused and often cave in to these sales agents. In the past, this might have been true. However, with the advance of comparison websites, Malaysians can now compare and find the best credit card to suit their individual spending behavior.

In conclusions, credit card debt issues are becoming more serious in Malaysia. Thus, a proper action should be taken in order to solve the problems. By studying the factor that influence people to use credit card and identify the effect of credit cards on customers spending behavior, I believe I can understand more background and behavior of the credit cards user in Malaysia.



Figure 1: Number of Credit Card holder in Malaysia

Based on the figure above, it shows the number of credit cards holder in circulation and ratio of credit cards holder in Malaysia. This shows that 1 in 3.48 Malaysians have a credit card which means most of Malaysians have their own credit card.

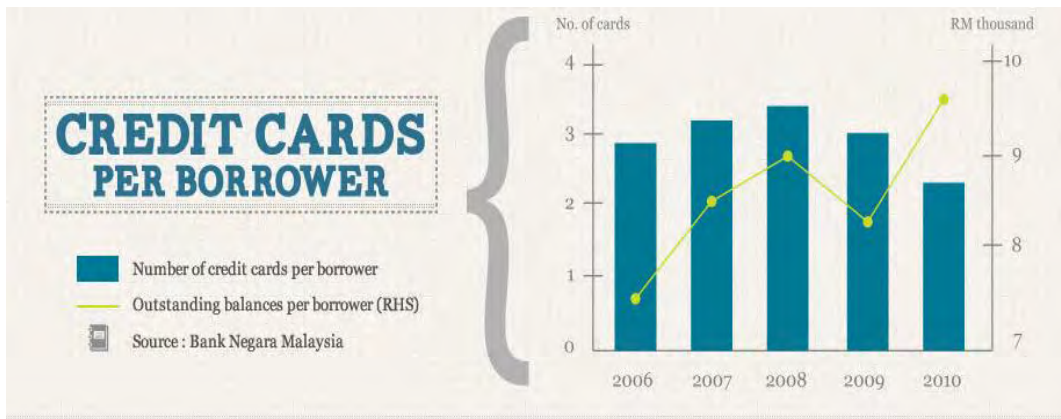


Figure 2: Statistics of credit cards per borrower and outstanding balances per borrower (RHS)

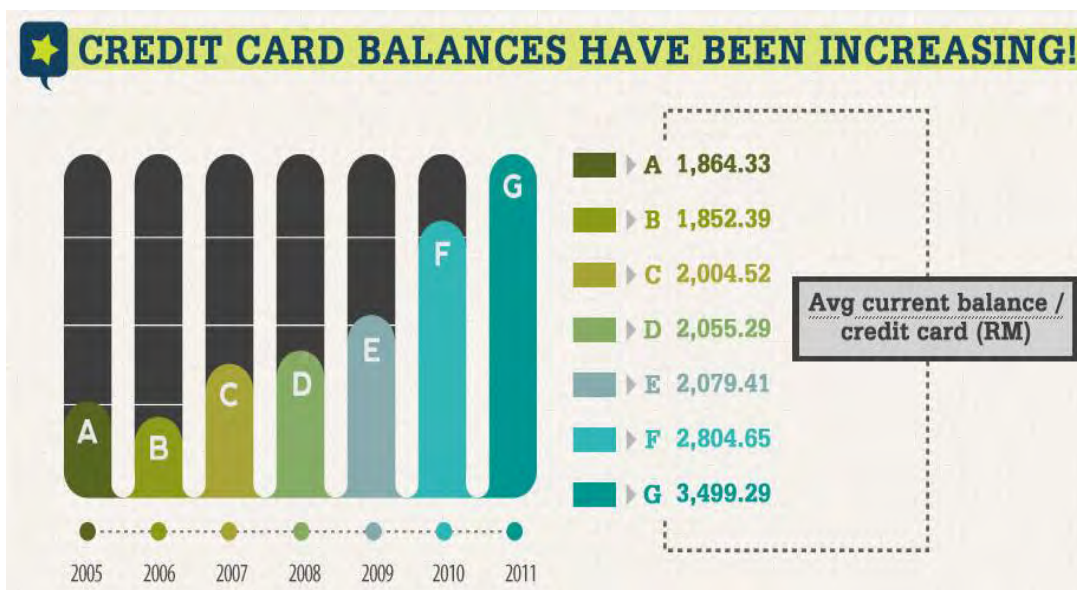


Figure 3: Average current balance of credit card

Based on the figure above, it shows that number of credit cards per borrower increase from 2006 to 2008. The outstanding balances per borrower also rapidly increase from 2006 until 2010. Moreover, the average current balance of credit cards has increase from 2005 until 2011. This statistic has shown us that most of people in Malaysia have gained their trust toward credit cards and they also keep increasing their outstanding balances.

### **2.2.3 Importance of credit cards in the economy**

Credit card is seems to substitute cash as a medium of exchange and purchasing mechanism. According to APACS's annual report (2004), around two thirds of adults have a credit card and multiple card has been as phenomenon in the UK. Credit does increase standard of living, manage emergency case, ease customers and increase expand market for business, (Mishler and Cole, 1998). There are eight reasons why people hold credit card: greater point's scheme, greater pricing, designation of credit card, promotions and offer, loyalty towards bank, prestige, credit limit enrichment and facilitates debt management, (P. Gerrard, S. Worthington and James F. Devlin, 2006).

According to HESSA (2009), credit card will give some problems in the future because it reassures people to borrow more. If an individual are not able to pay punctually, it would give an effect for he or she to get a job, takes other loan or automobile insurance because creditor have a tendency to to check customer's financial history. Consumers way of life has been affected because of the philosophy buy now and pay later. The behavior towards credit card use different from one customer to another depends on their level of concern, (R.A. Feinberg, 1986). According to Galanoy (1980), Merchants of Debt (1977), credit card has a relationship with spending. Customers will spend more if they use credit cards, (Burman 1974; Mathews and Slocum 1968). There are some factors influencing the credit card industry; as a main medium instead dependent on low profitability from operational costs and credit card markets in developing countries are not saturated yet, (Sook Yee Choo 2005).

### **2.2.4 Perception of people towards Banking**

Islamic Banking purpose is same like conventional banks, however the different between them is conventional banking products are interest based. The request for Islamic banking in Malaysia is started on 1969 limited as non-bank financial institution. .Therefore, in July 1983 first Islamic bank with the name of Bank Islam Malaysia Berhad was established and the Malaysian authorities have presented an Interest free banking scheme. Some banks market share have been increasing extremely starting past few years after offering Islamic credit cards using